

UNITED NATIONS



NATIONS UNIES

INTERNAL AUDIT DIVISION
OFFICE OF INTERNAL OVERSIGHT SERVICES

Reference: AUD-7-7:7 (0277/03)

30
22 March 2004

To: Mr. Rolf G. Knutsson, Executive Secretary
United Nations Compensation Commission,

From: Patricia Azarias, Director
Internal Audit Division I, OIOS

P. Azarias

Subject: **OIOS Audit Number AF2002/27/3 – Audit of UNCC F3 Claims: Part two of the Third Installment**

1. I am pleased to present herewith the final report on the subject audit, which was conducted in Geneva from February to September 2002. The audit was conducted in accordance with the standards for the professional practice of internal auditing in United Nations organizations.
2. The report incorporates as appropriate the UNCC Secretariat's comments on OIOS audit observations 938/02 and 939/02 issued on 23 September 2002. Concerning recommendations numbers 103, 104, 105, 106, 114, 126, 134, 139, 140, 141, and 144 contained in the audit observations, we note your comments that according to an Office of Legal Affairs opinion these recommendations fall outside of OIOS' proper scope of audit. OIOS does not agree with this assertion, and is reiterating these recommendations in this report. We request that you review the additional explanations contained in this report and provide us with your comments. Please note that OIOS considers all of the recommendations in this report as being of critical importance.
3. OIOS is assessing the overall quality of its audit process, and requests that you consult with your managers who dealt directly with the auditors and complete the attached client satisfaction survey form.
4. I take this opportunity to thank the management and staff for the assistance and cooperation provided to the auditors in connection with this assignment.

Copy to:
C. Bertini
Board of Auditors
M. Tapio, OIOS
D. Knutsen



United Nations
OFFICE OF INTERNAL OVERSIGHT SERVICES
Internal Audit Division

Audit Report

□ **Audit subject:** Audit of UNCC F3 Claims: Part two of the Third Installment

□ **Audit No.:** AF2002/27/3

Report date: 30 March 2004

□ **Audit team:** Bharat B. Manocha, Auditor

AUDIT OF UNCC F3 CLAIMS: PART TWO OF THE THIRD INSTALLMENT

EXECUTIVE SUMMARY

From February to September 2002 OIOS conducted an audit of Part Two of the third installment of "F3" claims. The UNCC Panel's report covers four claims of the Government of Kuwait, Ministry of Defense for losses totaling \$4.9 billion. The UNCC Governing Council considered the Panel's report in its 117th meeting held on 20 June 2002, and awarded \$2.1 billion to the Claimant. OIOS reviewed three of the four claims with an asserted claim amount of \$4.7 billion.

OIOS' findings were originally communicated as audit observations to the UNCC Secretariat on 23 September 2002. However, OIOS notes with regret that the Secretariat management's response was not provided until 11 April 2003. Moreover, a delay in the provision of essential working papers referred to in the consultant's report dated 14 December 2001 precluded OIOS from finalizing its review of the claim prior to it being presented to the Governing Council.

On the basis of the evidence and clarifications made available, OIOS identified the following deficiencies in the valuation and verification of the claims, which resulted in overcompensation to the claimants of approximately \$419 million. Figure 1 in the report provides a summary of the financial implication of OIOS' findings. The Secretariat has accepted errors amounting to approximately \$3.2 million. The deficiencies identified by OIOS are as follows:

- ❑ Overlapping claims for similar items resulting in double compensation;
- ❑ Certain cost savings not considered in some claims;
- ❑ Currency exchange errors;
- ❑ Calculation errors;
- ❑ Prices considered for compensation are higher than in the price list submitted by the claimant;
- ❑ Claim compensation made on insufficient evidence;
- ❑ Inadmissible claims; and
- ❑ Inconsistent application of recommended adjustments.

OIOS also observed that the quality control exercised by the Secretariat on the consultant's work was inadequate and needed substantial improvement.

In their response to OIOS' audit observations, the Secretariat stated that: "The proper scope of the OIOS audit has not yet been agreed upon by the Commission and OIOS, although it has been addressed in a legal opinion of the Office of Legal Affairs dated 27 November 2002 (the "OLA opinion"). This response addresses all of the observations and recommendations made, but does not respond to any draft observations that, consistent with the OLA opinion, extend beyond the proper scope of audit". In this regard the Secretariat did not respond to Recommendations 103, 104, 105, 106, 114, 126, 134, 139, 140, 141 and 144 contained in the audit observations. OIOS does not agree that these audit recommendations "extend beyond the proper scope of audit." This report comments on the Secretariat's response to the audit observations and reiterates OIOS' recommendations.

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LIST OF ABBREVIATIONS USED IN THE REPORT

Board of Auditors	BOA
Evidentiary Standard Matrix	ESM
Kuwaiti Dinar	KD
Ministry of Defence, State of Kuwait	MOD
National Guard	NG
Office of Internal Oversight Services	OIOS
Office of Legal Affairs	OLA
United Nations Compensation Commission	UNCC
United Nations Return of Property Programme	UNROP
Working Papers of the Consultant	WP

1. INTRODUCTION

1. From February to September 2002 OIOS conducted an audit of the Report and Recommendations made by the Panel of Commissioners concerning Part Two of the third installment of "F3" claims. The Panel's report covers four claims by the Government of Kuwait for losses totaling \$4.9 billion (excluding \$782 million of interest). The UNCC Governing Council considered the Panel's report in its 117th meeting held on 20 June 2002, and awarded an amount of \$2.1 billion¹. OIOS reviewed three of these claims --nos. 5000163, 5000181 and 5000192 with an asserted claim of \$4.7 billion of which UNCC awarded \$2.1 billion.

2. OIOS' consolidated findings were communicated to the UNCC Secretariat (Secretariat) as audit observations No. 939/02 and 938/02 dated 23 September 2002. The Secretariat's response was received on 11 April 2003.

II. AUDIT OBJECTIVES

3. The objectives of the audit were to determine if: (i) there were adequate controls to ensure compliance with decisions of the UNCC Governing Council; and (ii) the compensation awarded was appropriate.

III. AUDIT SCOPE AND METHODOLOGY

4. We test checked the compensability of the claims, the valuation and verification of the asserted losses by the Secretariat, the supporting evidence submitted by the claimants, and the Panel's recommendations on the compensation to be awarded. The Secretariat responded with regard to some of our findings that: *"The proper scope of the OIOS audit has not yet been agreed upon by the Commission and OIOS, although it has been addressed in a legal opinion of the Office of Legal Affairs dated 27 November 2002 (the 'OLA opinion'). This response addresses all of the observations and recommendations made, but does not respond to any draft observations that, consistent with the OLA opinion, extend beyond the proper scope of audit"*. In this regard, the Secretariat did not respond to recommendations 103, 104, 105, 106, 114, 126, 134, 139, 140, 141 and 144 contained in audit observations nos. 938/02 and 939/02. Since OIOS does not agree that these recommendations extended "beyond the proper scope of audit," as discussed below we are reiterating the original audit recommendations.

5. OIOS does not agree with the restrictions placed on its audit scope. Claims awarded constitute UNCC expenses, hence the audit of claims processing is fully within OIOS' scope. OIOS' mandate² is to "...review and appraise the use of the financial resources of the United Nations in order to guarantee the implementation of programmes and legislative mandates..." Furthermore, under Security Council Resolution 706(1991), funds from sales of Iraqi petroleum and petroleum products have to be deposited "into an escrow account to be established by the United Nations and

¹ S/AC.26/Dec.164 (2002)

² General Assembly Resolution 48/218 B (1994)

administered by the Secretary-General..." As a result, the use of these funds is a United Nations responsibility within OIOS' audit scope. Furthermore, the Board of Auditors (BOA) stated that the audit of claims is fully within the OIOS mandate because (i) the UNCC Governing Council is not of a "quasi judicial nature"; and (ii) the UNCC is managed by the United Nations Secretariat. As the internal auditor of the United Nations Secretariat, OIOS has internal audit authority concerning the management of UNCC assets.

IV. OVERALL ASSESSMENT

6. The deficiencies listed below relating to the valuation and verification of claims resulted in overcompensation of approximately \$419 million. Of this amount, the Secretariat has only accepted errors amounting to approximately \$3.2 million. A summary of the financial implications of OIOS' findings appears in Figure 1. The findings included the following:

- ❑ Overlapping claims for similar items resulting in double compensation;
- ❑ Savings such as those attributable to reduced maintenance costs resulting from the loss of those items for which the claim was made not considered in some claims;
- ❑ Currency exchange errors;
- ❑ Calculation errors;
- ❑ Prices considered for compensation higher than those in the price list submitted by the claimant;
- ❑ Claim compensation based on insufficient evidence;
- ❑ Inadmissible claims; and
- ❑ Inconsistent application of recommended adjustments.

Moreover, OIOS observed that quality control by the Secretariat of the consultant's³ work was inadequate and needed substantial improvement.

Figure 1: Summary of Financial Implication of Audit Findings

UNCC Claim No.	Nature of Loss	Amount Claimed	Amount Awarded	OIOS Recommended Adjustment
5000163	Ministry of Defense – ordnance stockpile losses	564,376,379	362,792,000	- 61,471,000
5000181	Ministry of Defense Navy Ships – equipment & facilities losses	383,970,593	163,307,000	-2,300,000
5000192	Ministry of Defense – Air Force tangible property losses	3,791,022,749	1,544,699,253	-355,435,000
<i>Total</i>		<i>4,739,369,721</i>	<i>2,070,798,253</i>	<i>-419,206,000</i>

³ UNCC contracted consulting firms to assist in the verification and valuation of the complex and larger compensation claims for losses suffered by corporations, government and international organizations.

V. AUDIT FINDINGS AND RECOMMENDATIONS

A. Delay in the provision of working papers

7. OIOS requested the Secretariat to provide the working papers referred to by the consultants in their final report dated 14 December 2001. OIOS needed the consultant's working papers to review the methodology applied and accuracy of the calculations in assessing the valuation of loss. OIOS' mandate⁴ provides that it has the authority of direct and prompt access to all records and documents necessary for its work. The delay in providing these papers adversely affected our work plan, which resulted in OIOS not being able to finalize the review of claim no. 5000192 before the Panel's report was considered by the Governing Council. A number of essential documents requested in our audit observation no. 939/02 dated 23 September 2002 have yet to be provided by the Secretariat.

8. UNCC Secretariat responded that: *"The secretariat takes issue with this observation. The working papers were sent to the auditor by e-mail on 27 and 28 June 2002, and a follow-up e-mail was sent on 29 June 2002, asking the auditor to confirm whether there were any documents requested that remained outstanding. That e-mail went unanswered. It was discovered on 1 August 2002 that the documents sent on 28 June had not been received, and the documents were resent on 2 August 2002. On 5 August 2002, in response to a member of the Team's expression of regret that some working papers were received only on 2 August 2002, the auditor's response was "no matter". He also confirmed in the course of that conversation that he had not yet looked at the working papers that had reached him by e-mail.*

9. OIOS wishes to emphasize that it initially requested the working papers on 26 April 2002. The request was repeatedly discussed, and at one point, the Secretariat informed OIOS that the request for the documents had been "put on hold." The Secretariat now states that the papers were forwarded to OIOS on 28 June 2002, which means that the records were made available more than two months later, by which time the Governing Council had reviewed the Panel's report and awarded the claim on 20 June 2002. However, OIOS' audit of the claim had been taken up before the Governing Council reviewed the Panel's report, so that the Council could also have taken OIOS' concern's into consideration when awarding the claim. Thus, the delay in providing the working papers defeated the purpose of OIOS' undertaking the review of the claim before the Council had considered the Panel's report. Further, regarding the comment that the auditor's response was "no matter" and that he had not yet looked at the working papers provided by e-mail, OIOS would also like to clarify that these remarks were made in an attempt to maintain a professional, courteous working relationship with UNCC Team members, who had apologized for the delay in forwarding the papers. OIOS regrets that its response is being used to justify delays in forwarding the working papers.

Recommendation 1

The UNCC Secretariat should in the future provide the consultant's working papers required for OIOS audits in a timely manner in order

⁴ Secretary-General's Bulletin ST/SGB/273 of 7 September 1994

to ensure that whenever possible audits can be completed prior to the UNCC Governing Council's review of the claim being audited (AF02/27/3/001).

B. Review of consultant's working papers

Consultant's working papers should fully support Panel conclusions

10. The Secretariat advised that they did not have (i) all of the evidence submitted by the Claimant and considered by the consultant in making their recommendations; or (ii) all the working papers relied upon by the consultants in making their recommendations. However, a Secretariat team conducted a review of the working papers in the consultant's office, which revealed that the consultant's working papers relating to the tangible property section for Claim No. 5000192 with a recommended award exceeding \$1 billion were "very poorly substantiated in terms of paperwork."

11. According to the Secretariat this deficiency was brought to the attention of the Panel of Commissioners, who directed the consultants to be careful in future. In view of the above findings on the quality of the consultant's working papers, it is not clear how the Secretariat concluded that further justification of the consultant's conclusion on the valuation of loss was not required. It is imperative that working papers are complete and support panel decisions. OIOS therefore recommended that the Secretariat establish appropriate procedures for reviewing consultant's working papers, and if the working papers do not support conclusions, the Secretariat request the consultant to perform additional work.

12. The Secretariat responded: *"That review is carried out as part of the secretariat's quality control function as regards the work of the expert consultants, so as to ensure that the work is of sufficient quality and in conformity with the Panel's instructions⁵. A quality control function is intended to involve a sample-based review of the consultants' work, and not to repeat the consultants' work in toto. In practice, the quality control function is exercised on a continuous basis during the entire claims review process, including the review of consultants' draft reports to the Panel, meetings to discuss relevant issues, and the joint preparation of memoranda for the Panel." The review comprises a sample check of the consultants' work, and not an audit thereof. The VVSB officers assigned to each installment design a review programme in advance, which checks whether the opinions selected are properly supported by the consultants' working papers. The secretariat*

⁵ The review of claims within the Secretariat is carried out by the Claims Processing Division, which includes the Legal Services Branch (LSB) and the Verification and Valuation Support Branch (VVSB), and the quality control function (carried out under the direction of the LSB Team Leader) is part of VVSB's mandate as set out in paragraph 2 of its Standard Operating Procedures (SOPs). The advice and recommendations of the consultants are therefore presented to the Panel only after the Secretariat has provided quality control input. The advice and recommendations so presented are therefore normally agreed upon by the Secretariat and the consultants (the questions raised in the OIOS memorandum do not touch upon any areas in which there were differing views). Accordingly, the Secretariat did not provide advice and recommendations different from those of the consultants referred to in this response. Nonetheless, it is assumed that the relevant VVSB staff reviewed the working papers underlying each item of advice and recommendation.

compiles full records of each such review, and presents its findings to the "F3" Panel, as it does with all results of the quality control of the consultants' work."

13. OIOS does not accept the Secretariat's response to the audit observation because in some claims the work asserted to have been carried out by the consultant was not documented. While the consultant referred to its discussion with the claimant and their defense specialist, these discussions and the analysis thereof were not documented in the consultant's final report to the Panel. Furthermore, the Secretariat and the consultant again stated that they did not retain a full copy of the document relating to the claim for \$177 million⁶ they reviewed during their mission to Kuwait. The consultants also took decisions on issues of overlapping claims which were not within their mandate.

14. Additionally, the value of the "quality control" exercised by the Secretariat needs to be reviewed considering that it apparently accepts any of the consultant's responses. For example, in its initial response to an OIOS observation on the incorrect valuation of Luna Rockets, the Secretariat disagreed with our recommendation based on the consultant's opinion. The Secretariat stated that *"After due consideration, we are satisfied that the consultants have fully addressed the matters raised in your query."* However, when OIOS reiterated the recommendation, the consultant as well as the Secretariat agreed that there was an error of \$1.8 million⁷. The Secretariat has not explained how its quality control system failed to understand this calculation error pointed out by OIOS.

Recommendations 2 and 3

The UNCC Secretariat should:

- (i) Establish appropriate quality control procedures to review the consultant's work done on all claims (AF02/27/3/002); and
- (ii) In cases where it determines that the consultant's working papers do not support conclusions, request the consultant to provide additional supporting evidence (AF02/27/3/003).

C. Claim 5000163 – Kuwait Ministry of Defence, ordnance stockpile losses

15. The Ministry of Defense (MOD) State of Kuwait asserted that its ordnance stockpiled in depots and in military unit armories was stolen or destroyed by Iraqi forces. The MOD claims it sustained losses amounting to \$564.3 million (excluding interest) as a result of these actions. It also stated that much of the original purchase documentation was destroyed, thus four key data compilations that survived the occupation were used to determine the loss. After its review, UNCC awarded \$362.8 million to the claimant. Figure 2 summarizes the adjustments recommended by OIOS as a result of its review of claim 5000163.

⁶ Refer paragraph 93 of Secretariat response 11 April 2003 Footnote 17

⁷ Paragraph number 67-70 of Rec. no. AF02/27/3/11

Figure 2: Claim 5000163 - Adjustments Recommended by OIOS (in US \$)

Nature of losses	Amount claimed (\$)	Amount awarded (\$)	OIOS recommended adjustment (\$)	Reasons for overcompensation/ OIOS comments	Recommendation accepted by UNCC?
Losses supported by the Control Form printout	419,746,367	279,131,000	-17,500,000	Incorrect application of prices	No
Losses supported by the Status Report printout	59,683,753	39,690,000	0	No adjustment recommended by OIOS	
Losses supported by the Order Receipt report	84,946,259	43,971,000	-43,971,000	Inadequate evidence of receipt of stocks	No
Total	564,376,379	362,792,000	-61,471,000		

Incorrect application of prices

16. The MOD's claim of \$419.7 million is supported by data in the Control Form compilation dated 2 days before the invasion. This shows the code number of each item of ordnance and the quantity of each item. The total cost of 240 items was determined by multiplying the quantity in the Control Form with the price for the item recorded in the Price List that survived the invasion. The Panel reviewed the claim and found that adjustments should be made for saved expenses (i.e. those costs for such items as maintenance and storage of goods which would no longer be incurred following the theft or destruction of the items) and insufficient evidence, and recommended compensation of \$279.1 million of the \$419.7 million claimed.

17. OIOS' test check revealed that the claimant did not apply the rate stipulated in the price list in six of the items, in quantifying the loss. While a rate higher than that recorded in the price list had been used in five of the items, a lower rate had been used for one item. Incorrect application of the price resulted in inflating the claim by approximately \$17.5 million.

18. UNCC noted: "*The secretariat concludes that it would be inappropriate to alter the amount of compensation recommended, because to do so would be to invalidate the use of the sample approved by the Panel. Furthermore, the apparent error identified by the auditor has been taken into account within the adjustment made for insufficient evidence, made in the application of the ESM. Accordingly, the secretariat is of the opinion that no adjustment should be made to the recommended award.*"

19. In OIOS' view, the Secretariat's response is not tenable because:

- (i) Its assertion that the errors identified are already covered by the adjustment of ESM is not correct because adjustments made for ESM⁸ relate to the evidence submitted by the

⁸ The consultant had prepared an Evidentiary Standard Matrix (ESM) for making adjustments against the amount claimed, if the evidence was inadequate to support the claim. This matrix was approved by the Panel of Commissioners.

claimant and do not include adjustments for calculation errors. This is substantiated by the fact that the Secretariat has agreed⁹ to two calculation errors valued at \$3 million (in claim 5000192) attributable to depreciation and exchange rate errors. If, the ESM adjustment covers risks of overstatement, then there was no justification for the Secretariat to have accepted these two calculation errors as they had been taken into account within the adjustment for insufficient evidence, made in the application of the ESM.

- (ii) In arriving at the recommended claim amount, the consultants corrected or adjusted other errors/deficiencies before applying the ESM adjustment. Therefore, if the consultants had detected the errors due to incorrect application of prices this would have resulted in:

- The calculation errors being deducted from the amount applied for the application of ESM; and
- Downgrading the classification of the evidence and consequently the ESM adjustment factor would have been higher and the net compensation amount even less.

- (iii) Finally, the statement implies that there is no need for quality control by the Secretariat or oversight by OIOS or the Board of Auditors – because any errors that may be pointed out would have already been considered by the application of ESM. This is contrary to good management practice and principles of accountability and governance and contravenes ST/SGB/2000/8 dated 19 April 2000, which requires that independent and effective system be established for monitoring implementation and effectiveness of the work actually done.

20. Therefore, the error was caused by the incorrect application of prices resulting in overstatement of the claim and is not related to insufficient evidence. This error falls under Article 41¹⁰ and should be corrected.

Recommendation 4

With regard to claim no. 5000163, the UNCC Secretariat should ensure that: (i) the correct prices are applied to quantify the claim amount supported by the Control Form; and (ii) the compensation is adjusted accordingly (AF02/27/3/004).

⁹ UNCC response dated 11 April 2003 to OIOS Audit Observation on "F3" Claims – claim no.5000192 - paragraphs 166 & 167

¹⁰ The Provisional Rules of the Claims Procedure

Losses supported by order receipt report

21. The MOD sought compensation of \$84.9 million for the loss of ammunition purchased in 1984. The claim was made on the basis of the 22 August 1989 Order Receipts Report, which summarizes a special purchase of ammunition. The consultant stated that the investigation revealed a 15.45 per cent delivery shortage against 9 of the 11 categories of ammunition. After making adjustments for inflation and savings in maintenance expenses, the Panel recommended an award of \$43.9 million.

22. OIOS' review of this claim revealed the following deficiencies in the evidence submitted by the Claimant:

- According to the Order Receipt Report, the quantities ordered were not received until 22 August 1989, the date of the computer printout report. Subsequently, the quantities outstanding were deleted and the quantities asserted to have been received inserted manually. There was no evidence of who authorized this alteration, when the alteration was made or whether it was based on adequate evidence. Considering that the items stated were received in October 1987 no justification has been provided to explain why these figures were still not incorporated into the database two years after receipt;
- Even if we accept the Claimant's assertion that the items were received, questions persist about the adequacy of the MOD's internal controls. Hence, placing reliance upon the computer printouts submitted as evidence for other claims, would be inappropriate;
- There was no collateral evidence that any of these items were received and were in stock on the date of the invasion of Kuwait;
- There is no evidence that payments had been made to the vendor for these deliveries; and
- As shown in Figure 3 below, quantities asserted to have been ordered and received contained discrepancies.

Figure 3: Discrepancies in Quantities Asserted to Have Been Ordered and Received

Description	Quantity ordered as per claim	Quantity accepted by the Secretariat as being received	Unit value (\$)	OIOS remarks
Fuse for RDS 125 MM	200	169	9,506	No item in Exhibit 6 ¹¹ for which 200 were ordered.

¹¹ Refers to Exhibit numbers submitted by the claimant

Gun Fire Simulator RDS	32,522	32,522	36,587	No item in Exhibit 6 showing that 32,522 were ordered and received.
Gun Fire Simulator CHG	50,000	42,275	31,706	No item in Exhibit 6 showing 50,000 ordered or 42,275 received
RDS 12.7 MM X 107, AP	495,000	373,312	182,185	The total number of items received was 448,552 compared with 373,312 shown.

23. Furthermore, for the purpose of evaluating the ESM factor, the claim for compensation of an \$84.9million loss supported by the Order Receipt report has been grouped with the claim for a loss of \$419.7million supported by the Control Form printout and a common ESM applied to both claims. In OIOS' view, the ESM factor applied for the loss supported by the Order Receipt report should be different than that for the loss supported by the Control Form Printout which has a higher evidentiary standard.

24. UNCC responded that: *"The secretariat is of the view that the query extends into an area that is, according to the OLA opinion, beyond the proper scope of an audit query. The secretariat therefore has not responded to the query in this response in so far as it extends to the assessment of the evidence, save to consider whether there has been any computational error in the consideration of the evidence. All the working papers for this claim have been provided to the auditor."*

25. The Secretariat did not respond to the specific deficiencies in the evidence pointed out in our audit observation. Regarding the errors, the Secretariat stated: *"The consultants therefore applied an adjustment for overstatement of 15.45 per cent against each of the 11 categories of ammunition (details recorded in their Working Paper 6502, and see also Document 6010), and a further adjustment for overstatement in respect of the price claimed (the two adjustments together totaling \$18,824,000). They also considered whether issued munitions were included in the claim, and (after having interviewed witnesses on mission in Kuwait and reviewed claim documents) concluded that there was no evidence to suggest that issued munitions were included in the claim."*

26. The Secretariat's response did not address the issue stated in OIOS' audit observation regarding the deficiencies in the quantity ordered and the quantity received. Also, the Secretariat has not provided any documentation or clarification concerning this issue.

Recommendation 5

OIOS reiterates its recommendation that in view of the deficiencies observed in the Order Receipt Report concerning claim no. 5000163, the UNCC Secretariat should ensure that: (i) an adjustment is made for inadequate evidence, and (ii) different ESM factors are applied for claims involving losses supported by the Order Receipt Report and those supported by the Control Form Printout (AF02/27/3/005).

D. Claim 5000181 – Kuwait Ministry of Defence, equipment and facilities

27. The Claimant asserted that it sustained losses as a result of theft or destruction of navy property including ships, equipment, facilities, and ammunition. The Panel reviewed the claims and found that adjustment should be made for saved expenses, inadequate accounting and insufficient evidence, and recommended compensation of \$163.3 million out of the \$384 million claimed. The Panel's adjustments and the adjustment recommended by OIOS are shown in Figure 4.

Figure 4: Claim 5000181 - Adjustments (in US\$) Recommended by OIOS

Nature of losses	Amount claimed	Amount awarded	OIOS recommended adjustment	Reasons for overcompensation/ OIOS comment	Recommendation accepted by UNCC?
Lost or damaged navy vessels	20,361,505	7,255,000	0	No justification for applying rate of inflation ranging Between 11-26% for valuing loss, which is much higher than 5% applied for other similar claims	No
Technical branch inventory & ammunition depot losses	158,668,638	87,506,000	-2,300,000	Expenses saved have not been adjusted	No
Exocet missiles & support equipment lost/damaged	56,253,415	19,466,000	0	No adjustment recommended by OIOS	
Losses of equipment & inventory in workshops & store areas	136,586,734	43,506,000	0	No adjustment recommended by OIOS	
Losses of equipment and inventory of other Navy Base divisions	10,762,710	4,707,000		No adjustment recommended by OIOS	
Real property	1,337,591	867,000	0	Not reviewed by OIOS	
Total	\$383,970,593	\$163,307,000	\$-2,300,000		

Inflation rate for valuing naval vessels higher than that applied to other claims

28. The claimant stated that it had adjusted the claims for naval vessels for inflation, and asserted that it had estimated that prices for naval equipment and supplies had increased by approximately 5 per cent annually. Accordingly, the Claimant adjusted the prices of the items in Claim nos. 5000163 and 5000181 by this inflation rate. The Panel accepted this rate, and compensation was adjusted accordingly. The Panel recommended compensation of \$5.7 million of the \$16.8 million claimed for naval vessels.

29. The claimant valued the loss of fire fighting tugs, landing craft and service launches on the basis of a quotation received from the original supplier. As the quotation was for the purpose of the

claim and not for intended procurement, the consultant adjusted the quoted prices downward by 15 per cent.

30. OIOS observed that the replacement cost considered for valuing the losses of these ships reflected a price increase ranging from 11 to 26 per cent annually. As the price increase for these ships is much higher than the rate of 5 per cent applied to other MOD claims, there should be appropriate justification for applying it. However, there was no documentation showing that the unduly high inflation rate of 26 per cent per year was considered by the Secretariat and found to be justified. The "F3" Claims Unit explained that the claim was based on the replacement cost, and the Panel's review was aimed at establishing whether the prices paid for the replacement were reasonable. OIOS maintains that if the annual inflation rate of 26 per cent, which is substantially higher than the inflation rate for similar claims, cannot be justified, the Claimant will have been overcompensated by a significant amount.

31. UNCC responded that *"The secretariat is of the view that the query, which challenges the Panel's assessment of the evidence and valuation approach, extends into an area that is, according to the OLA opinion, beyond the proper scope of an audit query. The secretariat therefore has not responded to the query in this response in so far as it extends to the identification of the correct rate of inflation to be applied, save to consider whether there has been any computational error in the determination of the rate."*

Recommendation 6

OIOS reiterates its recommendation that because appropriate justification for applying a higher inflation rate for valuing the fire fighting tugs, landing craft and service launches than that applied to similar claims has not been provided, the UNCC Secretariat should amend the inflation rate and adjust the compensation in claim No. 5000181 accordingly (AF02/27/3/006).

Incorrect application of ESM matrix factor for naval ships

32. The Panel approved an ESM proposed by the consultant for applying evidence to F3 claims, to ensure consistency in evaluating and verifying the losses. Considering the evidence submitted by the claimant, the consultant recommended an application of 30 per cent ESM factor for adjusting the naval ship claim. The Panel accepted this recommendation and adjusted the claimed losses by 30 percent.

33. However, OIOS noted that the classification of the evidence by the consultant should have resulted in an ESM factor of 40 per cent instead of 30 per cent applied which increased the compensation by approximately \$1 million. The "F3" Team informed us that they had also noted this inconsistency in the consultant's report and adjusted it. However, we observed that the documentation made available to OIOS (and the documents submitted to the Panel) had not been amended to reflect this correction. The "F3" Claims Unit informed OIOS that on the basis of further

review the evidence was reclassified as "Good" and hence, the ESM of 30 percent was appropriate. They added that the consultant omitted to make this correction in his final report and agreed to provide the relevant documents to OIOS, which have not been provided to date.

34. UNCC responded that: *"The auditor's statements are correct, in that the secretariat discovered an error in the recording of the classification of the evidence during the course of the review process, and the error was discussed with the consultants. The consultants confirmed that the error was typographical. The percentage adjustment in the table in the consultants' report applying the ESM was correct, at 30 per cent, though the description of the evidence was not, and consequently the error was a simple clerical one and not one arising from the reconsideration of the evidence itself. It was brought to the attention of the Panel, which approved the (correct) amount of the adjustment. The error has been corrected in the documents, and the relevant pages provided to the auditor. There is, therefore, no error in the amount of compensation recommended by the Panel. The secretariat has therefore concluded that there is no justification for re-considering the application of the ESM to this head of claim."*

35. OIOS reiterates that the corrected document was not made available for OIOS' review. This issue was raised in the meeting with the Secretariat in April 2002 where they agreed to provide the explanation/documentation. The information was again requested in May 2002 through E-mail, and was also discussed with the Secretariat at a meeting in August 2002. The Secretariat in its response dated 11 April 2003 stated: *"that the error has been corrected in the documents and the relevant pages provided to the auditor."* However, OIOS has not received this documentation.

Ammunition stores losses - no provision for saved expenses

36. The claimant asserted that it had sustained losses of \$38.7 million for the cost of naval ordnance stored at the naval base or on board naval ships stolen or destroyed by the Iraqis. The Panel recommended \$19.8 million as compensation.

37. OIOS found that the estimated savings in general maintenance costs for the ammunition had not been deducted from the compensation recommended. Considering provisions approved by the Panel for similar claims, an adjustment of 2.5 per cent of the replacement cost per annum, extended over 4 years should have been made. Accordingly, the saved expenses would total approximately \$3.9 million. After adjusting for the 40 per cent ESM factor, the net claim recommended should have been \$17.5 million instead of the \$19.8 million approved. The failure to provide for the saved expenses resulted in net overcompensation of \$2.3 million.

38. In their response UNCC stated: *"The consultants did not recommend an adjustment for saved maintenance expenses in respect of the ammunition stores losses, and the Panel accepted the consultants' advice and recommendations. The secretariat has found no evidence that would justify any alteration in the advice and recommendations made."*

39. The Secretariat's response contradicts its own recommendations for savings of maintenance expenditures approved in claim numbers 5000192 and 500181. Although the Secretariat asserts that

no maintenance was required for spares parts, general supply stores, furniture and fixtures and computer equipment, it had proposed savings for all these items as reported below:

(i) The same claimant claimed \$119.99 million for losses of spare parts in the Technical Supply Branch¹². The consultant recommended and the Secretariat approved savings in operational costs of \$7.2 million. The spare parts included electrical, electronic and mechanical items, gasses, paints and chemicals, heavy equipment, lubricants and greases and other miscellaneous spare parts.

(ii) The claimant claimed \$784,000 for spare parts and furniture and fixtures in claim no. 5000192. In their final report (para. 6.302) the consultants stated, "We have applied normal adjusting principles in the appropriate parts of the General and Specific Verification Programmes and made a deduction of \$39,000 for savings in maintenance (furniture & fixtures).

40. Normally, storage of any stores involves some maintenance costs in terms of space, security, upkeep, certification, etc. While the Secretariat has approved savings in operational costs for spare parts for naval vessels, furniture and fixtures, etc. there was no justification as to why savings should not be made for naval ordnance, which has to be kept in readiness for any eventuality, and for which the maintenance costs is expected to be higher.

Recommendation 7

OIOS reiterates its recommendation concerning claim no. 5000181 that the UNCC Secretariat make adjustments for savings in general maintenance costs for naval ordnance stored at the naval base or on board naval ships and that the net compensation payable be adjusted accordingly (AF02/27/3/007).

Losses of equipment and inventory in other Navy base divisions

41. The claim included \$4.37 million for military assets. In applying ESM for this claim the consultant recommended a factor of 20 per cent (based on their WP6504) and the claim was adjusted accordingly. However, based on the worst evidence in WP6504 (again assessed on loss/damage) the ESM was assessed at 30 per cent since it was standard practice for a claim to be adjusted on the basis of the worst evidence. This discrepancy in the application of the ESM should be clarified.

42. *The Secretariat commented: "The consultants advised that "[t]he 'Worst Evidence' recorded on the working paper was 30%. However, this was not supported by the detail set out in the working paper. The correct ESM based on the working paper is in fact 20%, because the evidence quality under the heading Loss/Damage was rated as "good". In other words, we did apply the correct ESM factor of 20% as set out in the Final Report itself." Accordingly, the consultants conclude that "the 30% deduction in the working paper is a clerical error", and that "this error was not*

¹² Kuwait MOD claim - UNCC Claim no. 5000181

duplicated in the Final Report". "The secretariat, having re-checked the working papers and the Final Report, concurs with the consultants' conclusions. Therefore no alteration to the advice and recommendations in respect of this head of claim is warranted."

43. OIOS acknowledges that *"this error was not duplicated in the Final Report"*, nevertheless, the working paper does not support the ESM factor applied in the calculation. It would therefore also be appropriate to correct the error in the working paper. The corrected document should be kept on record for future reference.

E. Claim 5000192 – Kuwait Ministry of Defence, Airforce tangible property

44. MOD claimed that the Iraqi forces stole and destroyed planes, armament, air defense systems, ground equipment, communications systems, technical manuals, several air force buildings, and other real property. The invasion also interrupted construction projects previously commenced. Furthermore, vehicles, communications systems, artillery and other property belonging to the Land Forces and Navy were also destroyed. MOD claimed that losses were also incurred because many employees did not report to work during the occupation. The claimant sought compensation of \$3.79 billion for the losses and damage. UNCC reviewed the claims and after making adjustments, awarded \$1.54 billion to the claimant. Figure 5 sets out the nature and financial implications of the adjustments resulting from OIOS' audit findings.

Figure 5: Claim 5000192 - Adjustments Recommended by OIOS (in US \$)

Nature of losses	Amount claimed	Amount awarded	OIOS recommended Adjustment	Reasons for overcompensation/ OIOS comments	Recommendation accepted by UNCC?
Spare parts & armaments	46,406,584	32,543,000	0	No adjustment recommended by OIOS	
Bombs & missiles	12,731,717	5,888,000	0	Not reviewed by OIOS	
Aircraft & aircraft engines	122,018,489	59,131,000	0	No adjustment recommended by OIOS	
Air defense systems	898,922,383	445,998,000	-214,900,000	Inadequate evidence for reimbursement (service & support costs reimbursed which are not reimbursable)	No
Air defense systems			-3,353,000	No evidence that claimant paid the vendor and thus incurred the loss	No
Air defense systems			-27,300,000	No evidence of existence or damage	No
Air defense systems			-2,895,000	UNCC accepted net amount of \$1,515,000	Yes
Air defense systems			-2,072,000	Savings in expenditure not provided for	No
Command, control & Commun.systems	233,745,984	75,302,000	0	No adjustment recommended by OIOS	

Automated supply system	70,628,113	25,353,000	0	No adjustment recommended by OIOS	
Ground equipment	10,758,308	5,455,000	0	Not reviewed by OIOS	
Technical books & manuals	5,518,874	1,046,000	0	Not reviewed by OIOS	
Mine clearance equipment	8,382,197	1,212,000	0	Not reviewed by OIOS	
MEP tangible property	18,017,724	4,505,000	0	Not reviewed by OIOS	
Vehicles	182,534,161	30,850,000	0	Not reviewed by OIOS	
Tanks & armored vehicles	577,809,795	190,669,000	0	No adjustment recommended by OIOS	
Artillery	117,587,631	14,611,000	-14,284,000	Overlapping claim for items claimed in Claim no. 5000163	No
Artillery			-1,719,000	Accepted by UNCC	Yes
Other equipment	498,498,963	332,162,000	-24,912,000	Expenses saved have not been adjusted	No
Wire & wireless communication eq.	107,248,666	41,069,000	0	No adjustment recommended by OIOS	
Communications equipment, etc	65,425,806	42,149,000	0	No adjustment recommended by OIOS	
KERP adjustment	-33,354,747	-33,354,747	0	Not reviewed by OIOS	
MEP reconstruction costs	439,026,559	228,411,000	-64,000,000	Overlapping claim - inadequate evidence	No
MEP Contract	1,559,897	558,000	0	Not reviewed by OIOS	
Total	3,791,022,749	1,544,699,253	-355,435,000		

Land forces (Other Equipment) - no provision has been made for saved expenses

45. The claimant sought compensation for the loss of other equipment owned by the Land Forces such as vehicle spare parts, bulldozers, graders, chemical defense equipment, technical stores, etc. The total claim was for \$498.5 million. The Secretariat awarded \$332.16 million as compensation after making adjustments for inflation, depreciation and insufficiency of evidence.

46. OIOS observed that no adjustment was made for saved expenses for this equipment. Since this equipment was either stolen or otherwise destroyed, the claimant would not have incurred expenses that it would ordinarily have incurred. The Secretariat has adjusted savings in other similar cases. Therefore, the same adjustment should have been made for this claim also. We requested the Secretariat to provide us with MOD's reply dated 15 January and the translated schedule of type of vehicles.

47. In its response the Secretariat stated that: *"The consultants have advised that they recommend adjustments for saved expenses where they are satisfied that actual savings had, or should have been, achieved in connection with the property concerned. In order to come to such a conclusion, the consultants seek evidence of pre-invasion relevant expenses, and evidence as to whether such*

expenses continued after liberation. In cases in which the claimant was unable to provide evidence of relevant maintenance expenditure, the consultants used normal industry standards in their assessments."

48. The Secretariat's response contradicts its own recommendations for savings of maintenance expenditures approved in claim numbers 5000192 and 5000181. Although the Secretariat asserts that no maintenance was required for spares parts, general supply stores, furniture and fixtures and computer equipment however, it has proposed savings for all these items as described in paragraph 38 of this report. Considering the provisions approved by the Panel for similar claims, an adjustment of 2.5 per cent per annum for 3 years should have been made. In OIOS' view, failure to provide for the saved expenses has resulted in net overcompensation of \$24.9 million.

49. Thus, the Secretariat has made provision for savings in operational costs for claims for spare parts, furniture, workshops, etc in the same claim (no. 5000192). However, it now asserts that there will be no savings on operational costs for similar equipment owned by the land forces. Therefore, in OIOS' view there was no justification for not providing for savings in operational costs.

50. Normally the storage of computers, stores and other items involves some maintenance costs for space, security, upkeep, certification, etc. When the item involved is for use by the army and required to be kept in readiness for any eventuality, the maintenance cost is expected to be higher. It is therefore difficult to understand why there were no savings on maintenance costs. The savings in maintenance costs should have been adjusted in calculating the compensable amount.

51. While the Secretariat forwarded the translated schedule of vehicle types to OIOS the MoD reply dated 15 January, which OIOS had previously requested, was not forwarded with the Secretariat's response dated 11 April 2003.

Recommendation 8

OIOS reiterates its recommendation that the UNCC Secretariat should make appropriate adjustments for saved expenses on other equipment in Claim No. 5000192 (AF02/27/3/008).

Overlapping claim for artillery

52. OIOS noted that there were overlapping claims for some artillery pieces such as 155 French guns and mortars in claim numbers 5000192 and 5000163 resulting in double compensation. The claimant claimed \$143 million (Exhibit 1E-4) for various artillery pieces as shown in Figure 6 below:

Figure 6: Artillery Items Included in Claim 5000192

Description	Qty.	Unit price (KD)	Total cost in KD	Total cost (US\$)
Type 155 French Guns with attachments	18		27,000,000	89,775,000

Mortars 120 MM	18	96,000	1,728,000	5,745,600
Mortars 81MM American & British	48		751,680	2,499,336

Source: Exhibit 1E-4 submitted by claimant

53. The Claimant also made a claim for the artillery items in Claim no. 5000163 (Figure 7):

Figure 7: Artillery Items Included in Claim 5000163

Code no.	Description	Qty.	Unit price (\$)	Total cost (KD)	Amount claimed (KD)*
125	Mortar 81 mm English	30	3,858	115,740	136,718
125	Mortar 81 mm English	100	2,382	238,200	281,374
126	Mortar 81 mm M29A1 American	51	3,903	199,053	225,614
150	Mortar 120 mm French	4	37,442	176,913	181,070
150	Mortar 120 mm French	10	14,976	176,904	175,594
160	Artillery Gun 155 mm RT HOW French	13	225,530	2,931,890	3,463,2953

* After adjustment for inflation and depreciation.

54. A comparison of the two claims revealed the following:

- a) The 155 mm French guns claimed in Claim 5000192 were procured from Creusot-Loire and refer to the same Contract no. KU/8-3/8 as claimed in 5000163;
- b) The cost of the 155 mm French guns (procured under the same contract) claimed was different in the two claims;
- c) The 120 mm and 81 mm mortars claimed in Claim 5000192 appeared to be similar to those claimed in Claim 5000163; and
- d) The price of the 81 and 120 mm Mortars in Claim 5000192 was estimated while that in Claim 5000163 was taken from the "Price List of Arms & Ammo" submitted by the Claimant. The price claimed in 5000192 was inflated, and needed to be adjusted. Applying the prices in claim no. 5000163 to the total cost of the guns, results in the compensable claim being overstated by more than \$5 million.

55. As the same artillery was claimed in two claims (5000192 and 5000163) with different prices, inflation factors and depreciation rates, OIOS requested the Secretariat to clarify the reasons for the overlapping claims and why different prices were applied to the same items. *The Secretariat responded: "As items with similar descriptions had been claimed in claim number 5000163, the consultants sought to establish whether the two claims overlapped. The documents submitted in support of MoD claim number 5000163 noted that the artillery claimed in claim number 5000163 related to "ordnance stockpiled in central depots located around the country and in military unit armoires" and, according to the Statement of Claim, the items claimed did not include any ordnance*

issued to the various sections of the Armed Forces¹³."

56. Furthermore the Consultants, "were satisfied that Kuwait had lost more than the 18 guns claimed in claim number 5000192 and 13 claimed in claim number 5000163, and that there was no duplication between the two claims as regards those guns¹⁴."

57. OIOS does not agree with the Secretariat's response, which stated that the "the consultants advised the Panel that they were satisfied that Kuwait had lost more than the 18 guns claimed in claim number 5000192 and 13 claimed in claim number 5000163, and that there was no duplication between the two claims as regards those guns." If the consultant had noted the overlap, and considering that the amount involved was \$90 million, this discrepancy should have been raised with the claimant and a formal response requested as was done in the case of the Luna Rockets (the consultant noticed an overlap in Luna Rockets of \$14.4 million). The claimant should have been asked to clarify this situation and the consultant should have reported this overlap in his final report. However, this duplication involving artillery was not documented in the records made available to OIOS. Even the consultant's final report dated 14 December 2001 made no reference to this duplication. Considering that the amount involved was \$90 million, it was imperative to bring this possible overlap to the Panel's attention. In OIOS' view, the consultant had no mandate to decide if there was or was not an overlap.

58. From the documents recently received from the Secretariat (translation schedule of the type of vehicles) the claimant sought compensation for 155mm guns in the list of vehicles. Therefore, it is possible that the guns were also claimed and compensated in that claim.

59. Concerning the overlap of 120mm and 81mm mortars, the Secretariat responded:

"The consultants therefore advised that there was no duplication between the artillery claims in claim numbers 5000163 and 5000192. The evidence of existence of the artillery in each claim was based on the documents available, and the evidence of witnesses, was subject to the standard review under the "Guidelines for the Application of Evidentiary Standards". The secretariat has concluded that there is no evidence that would undermine the consultants' advice."

60. The reasons asserted by the Secretariat for the 120mm mortars are not plausible because:

¹³ The claimant itself noted the possibility of duplication in the statement of claim, stating that items in this claim were not duplicated in any other MOD claim. The Supplemental Statement of Claim filed for each "F3" claim includes an exhibit describing the standard procedures used by the advisors to the claimants to avoid double counting.

¹⁴ The auditor has made a reference to the same contract being supplied as evidence in support of the two claims for 155mm guns. The contract was used as evidence of existence of the guns claimed in claim number 500163, but not as evidence of existence in claim number 5000192. The value of French guns used in claim number 5000192 was based on a post invasion invoice for superior weapons, and the consultants sought further evidence of value. They were referred to the contract as evidence of the pre-invasion unit cost of 155mm French guns, and accepted that this contract was good evidence of general historic purchase cost of 155mm French guns. The consultants did not accept the contract as evidence of the existence of the 155mm guns claimed in claim number 5000192.

- In his final report the consultant stated: "the balance of the items comprise mortars, rockets launchers and "Luna" rockets. We have found no specific reference in our independent research but the equipment is of a type we would expect MoD to have held."
- If the consultant had noted the overlap and considering that the amount involved was \$8 million, which exceeded the materiality amount of \$500,000 proposed by the consultants¹⁵ and approved by the Panel, this should have been raised with the claimant and their response requested as in the case of the Luna Rockets.
- As mentioned, in OIOS' view, the consultants did not have the mandate to decide on overlap or duplication. This overlap should have been brought to the attention of the Panel for their consideration. No evidence has been made available showing that this was done, and hence the consultant has exceeded his mandate.

61. Regarding the issue of differences in prices, inflation factors and depreciation rates, the Secretariat responded: *"The consultants advised that the use of such a composite index, made up of many similar items, might be inaccurate when applied to any specific individual item. In claim number 5000192, when looking at the claim item of French guns alone, the consultants considered that no provision for inflation was justified. A unit price for French guns in 1990 of \$1,063,000 was, therefore, taken. The difference between the two unit prices used is \$117,000 per gun, which arises as the guns in claim number 5000163 were calculated as part of a composite claim item and those in claim number 5000192 were calculated at a specific unit rate."*

62. The consultant's response that differences in prices in the two claims are due to calculation as a composite claim item in claim 5000163 and at a specific rate in claim 5000192 was incorrect. The consultant reviewed the prices of each material item in this claim, and adjusted the prices for inflation, overstatement, etc. After adjusting the prices, the consultant recalculated the asserted loss as shown in their working papers. Hence, if the consultant had noted the difference in prices in the two claims, they should have adjusted the price in claim#5000192 and the revised loss valuation and submit it as a recommendation to the Panel for consideration as this was considered at a specific rate. It is relevant to note that in another similar item, the consultant did adjust prices for Luna Rockets (in claim #5000192). No justification has been provided for this contradictory treatment.

63. The Secretariat response is also not tenable because:

- Although the consultant asserts that the difference per gun was only \$117,000, the total difference for the 18 guns of more than \$2 million (117,000 x 18) substantially exceeded the materiality amount of \$500,000 proposed by the consultants¹⁶ and approved by the Panel. Hence, if the consultant had noted the difference this should have been reported to the Panel. The consultant had no mandate to decide on the duplication. Given that the overlap was neither reported nor the prices adjusted as

¹⁵ Guidelines for the Application of Evidentiary Standards Preliminary Report to the F3 Panel & Secretariat (paragraph 1.29)

¹⁶ Guidelines for the Application of Evidentiary Standards Preliminary Report to the F3 Panel & Secretariat (paragraph 1.29)

was done for the Luna Rockets leads to the inference that the duplication was not detected by the consultant or by the Secretariat.

64. Concerning different depreciation rates applied to the same guns, the Secretariat responded: *"Similarly, the depreciation factors used in claim number 5000163 for French guns were calculated using a composite depreciation rate for that loss element, based on the average age of all of the equipment included within that loss element (i.e. five years) and an average useful life of 40 years. The consultants advised that the approach was appropriate for the consideration of a composite claim, comprising items that had been contained in the stockpile for a considerable period, rather than specific, individual items in everyday use in the field. In claim number 5000192, the useful life was reduced to 25 years as the artillery was of one specific type, that is the French guns alone, and related to artillery in day-to-day use."*

65. The reason given by the Secretariat to justify the different rates of depreciation is not acceptable because in his final report the consultant stated, *"MOD claim that the useful life of the equipment was 25 years. This estimate is reasonable. The equipment is of the same genre as that in 'Military Assets' and our researches confirmed the reasonableness of the estimate."* There was no analysis or documentation showing that because the guns were used in the field, their life span would be different from that claimed in the claim 5000163. Moreover, the consultant has attempted to justify the use of two different useful lives (40 years and 25 years) for similar assets by asserting that some assets had been in stockpile for a considerable period rather than in everyday use in the field. This reflects a misinterpretation of the depreciation concept.

66. If the consultant had noted the different life spans for the same gun, (40 years in claim 5000163 and 25 years in claim 5000192) this should have been documented and the Panel informed. No evidence has been identified that this was done. As mentioned earlier, it is the consultant's responsibility to inform the Panel of these differences in claims to enable the Panel to decide on the compensation to be awarded. The discrepancies pointed out above indicate that the consultant failed to detect the overlap of the similar guns with different life spans.

67. Concerning the different prices for the 120mm and 81mm mortars the Secretariat concluded: *"the consultants have taken different unit prices for French guns, and in the case of all the artillery at issue, the inflation and depreciation rates applied in claim numbers 5000163 and 5000192 are different. The reasons for the differences are explained in paragraphs 54 to 57 above. The secretariat is of the opinion that the consultants' actions were appropriate in the circumstances, and follow the procedures laid down by the Panel. The secretariat therefore concludes that the amounts recommended should not be altered to conform to? unit prices, inflation and depreciation."*

68. In OIOS' view, the Secretariat's reply is not justified for the following reasons:

- The consultants advised that the prices claimed were not unreasonable for replacement in 1990. However, as shown in Figure 7, the replacement prices varied from 250 to 650 per cent higher than the original prices. The consultant adduced no reason why these unusually high prices were not considered unreasonable. The

unusually high prices should have been reported in the consultant's final report and brought to the Panel's attention.

- The high inflation rates also contradict the consultant's own assertion that: *"The evidence of the US Census Bureau is that military equipment prices were falling over the period although we do not know the precise specification for the equipment sold to Austria). However, we consider that it is reasonable to exclude the adjustment for inflation included in the claim."* The consultant did not allow any provision for inflation in the working sheet (WP6522). Thus, there is no justification for this response.

Figure 8: Variation in Prices for Same Items in Different Claims

Description	Price per gun in claim 5000192 (\$)	Price per gun in claim 5000163 (\$)	Difference per gun (\$)	Difference per gun (%)	No. of guns	Total difference (\$)
	(1)	(2)	(1-2)			
Mortar 120 mm	319,200	49,800	269,400	641%	10	2,694,000
Mortar 120 mm	319,200	124,500	194,700	256%	4	778,800
Mortar 81 mm	52,070	7,920	44,150	657%		
Mortar 81 mm	52,070	12,830	39,240	406%	48	1,883,520

- The Secretariat asserts that based on the advice received from the Kuwaiti Army personnel during the consultant's visit, the Secretariat concluded that the 120mm mortars claimed in the two claims were different and hence there was no overlap. However, it is the Panel's mandate to decide if there was any overlap. If the consultants had noticed that the same 120 mm mortars had been claimed in two other claims and there was no evidence to prove that they were different guns, this fact along with their recommendations should have been brought to the attention of the Panel for their consideration (as was done in the case of Luna Rockets). Therefore, the consultants exceeded their mandate.

Recommendations 9 and 10

The UNCC Secretariat should:

- Clarify why the consultant exceeded his mandate by deciding on the overlapping claims for the 155 French guns, 81 mm and 120 mm Mortars in claim nos. 5000192 and 5000163, and failed to report his findings to the Panel (AF02/27/3/009); and
- Make appropriate adjustments in the claim amount compensable to the claimant as a result of overlapping claims on 155 French guns, 81 mm and 120 mm mortars (AF02/27/3/010).

Incorrect calculation resulting in overcompensation for Luna rockets

69. The consultant amended the claim of \$14,400,000 for LUNA rockets in Claim no. 5000192 to \$10,232,000 (refer to their WP 6522) in accordance with the information in Claim no. 5000163. However, the consultant did not deduct the overstatement of \$4,168,000 from the total claim amount resulting in overcompensation to the claimant. Hence, OIOS recommended that the amount compensated be adjusted.

70. The Secretariat responded: *"The consultants have confirmed that an error was made. The value of the Luna Rockets was correctly stated at a total of \$14,400,000, but the depreciation adjustment should have been calculated at \$7,200,000 (not \$5,116,000 as stated). The depreciation is therefore understated by \$2,084,000."* *"The recommended award was \$36,613,000 whereas this should have been \$34,894,000. The overstatement in the recommendation is therefore \$1,719,000."*

71. In their initial response of 19 July 2002 to our observation, the consultant responded that their calculation was correct and that *"It would appear that the auditor has simply misunderstood the information..."*. Furthermore, the Secretariat agreed with the consultant's view and stated *"After due consideration, we are satisfied that the consultants have fully addressed the matters addressed in your audit query and we are in agreement with the consultants responses"*.

72. OIOS acknowledges that the consultant and the Secretariat have ultimately accepted the error. However, this raises the issue of the quality control conducted by the Secretariat on the work of the consultants¹⁷. If the secretariat had conducted a proper review, it should have understood the error when first pointed out by OIOS. There is a need for the Secretariat to investigate the reasons for this failure and to take appropriate action. The secretariat also needs to improve its quality review process (see Recommendation 2).

Overlapping claims for Luna warheads

73. A claim for Luna warheads had been made in both Claim 5000163 and Claim 5000192 as shown in Figures 9 and 10:

Figure 9: Price of Luna Warheads in Claim No. 5000163

Description	Country	Quantity	Cost (\$ 000)
Missile Luna HE warhead	USSR	111	11,445
Missile Luna practice	USSR	12	838

Source: Exhibit no. 1B-1

¹⁷ Refer paragraph 9 of UNCC response dated 11 April 2003

Figure 10: Price for Luna Warheads in Claim No. 5000192

Description	Country	Quantity	Cost (\$ 000)	Exhibit
Luna Rockets	USSR	120	14,400	1E-4

74. Since both the Luna rockets and Luna warheads were procured from the USSR and the number claimed is almost identical, there is a possibility that the claimant may have claimed for the same warheads twice. OIOS recommended that the Secretariat determine if the Missile Lunar HE warheads claimed in 5000163 were different from those claimed in 5000192.

75. The Secretariat responded that: *"The consultants advised that there was no duplication between the Luna Rockets claimed in claims 5000163 and 5000192. The secretariat concludes that there is no evidence that would undermine the consultants' advice."*

76. However, the Secretariat's response does not explain the following aspects:

- The consultant stated that Luna warheads were claimed in claim 5000163 and that claim 5000192 related to the missile part only. Furthermore, the consultant's defense specialist advised that the price of \$120,000 was reasonable for the rocket alone. The consultant adjusted the price of the Luna rocket for claim 5000192 to \$85,270 in accordance with claim no. 5000163¹⁸. If the two claims were for different parts, there was no justification for the consultant to amend the price to \$85,720 in claim 5000192 since it pertained to the missile only.
- Furthermore, no reason was provided as to why the consultants overlooked their specialist's advice that the price of \$120,000 was reasonable and adjusted the price to \$85,270.

Application of ESM evidence to field artillery

77. For the purpose of applying the ESM19 for Field Artillery, the Secretariat has accepted the classification of "type of evidence" as "primary" on the basis of the Damage Assessment Report and the "quantity of evidence" as "complete" as it covers all items. However, this classification is inappropriate for the following reasons:

- The Damage Assessment report does not fall within the primary evidence

¹⁸ Refer the consultants WP6522 for claim no. 5000192

¹⁹ The Panel adopted Guidelines for the Application of Evidentiary Standards. The Guidelines explain that an adjustment for insufficient evidence (one of a series of standardised amounts) is made against the amount claimed if the Panel considers that there is a risk of overstatement in the claim, for whatever reason. The adjustment is made by reference to the Evidentiary Standards Matrix ("ESM"). Sufficiency of evidence is considered with reference to whether the evidence relates to the pre-invasion period, the occupation and emergency period or the period thereafter, whether it is primary, secondary or tertiary, its quality (good, average or poor), and whether it is complete, partial or limited (and whether supported in the latter two cases).

classification approved by the F3 Panel which is "basically an original document; or a copy of an original; physical evidence (i.e. a building or vehicle); or photographic evidence."

- Classification of the evidence as "Complete" is inappropriate because evidence for 50 per cent of the admissible claim has not been provided by the claimant.

78. In response, the Secretariat forwarded the consultant's clarification, which explained that: *"In case of loss - best evidence available is generally a witness statement." "In all cases the damage assessment report has been found to be an accurate reflection of the loss (on the basis of sample check)." "In the circumstances we have taken the view that for this property the damage assessment report should be classified as primary evidence of loss or damage."*

79. While the Damage Assessment Report and the witness statement may be the "best evidence available" they were neither original nor physical evidence and hence, cannot be classified as primary evidence in accordance with the criteria accepted by the Panel. Since the consultants used a sample check to convert "secondary evidence" to "primary evidence" we requested that the Secretariat provide the complete details of the sample check conducted by the consultants on the basis of which the Damage Assessment Report was classified as "primary" evidence. This was necessary, since in a number of other MoD claims the Damage Assessment Report has been considered as "secondary".

80. The Secretariat responded that: *"The secretariat notes that the auditor is questioning the assessment of evidence by the Panel, which assessment is carried out under article 35(1) of the Rules. That article provides as follows: Each claimant is responsible for submitting documents and other evidence which demonstrate satisfactorily that a particular claim or group of claims is eligible for compensation pursuant to Security Council resolution 687 (1991). Each panel will determine the admissibility, relevance, materiality and weight of any documents and other evidence submitted. (emphasis added)." "The secretariat is of the view that the query extends into an area that is, according to the OLA opinion, beyond the proper scope of an audit query. The secretariat therefore has not responded to the query in this memorandum, save to consider whether there has been any computational error in the consideration of the evidence. All the working papers for this claim have been provided to the auditor." "The secretariat concludes that the auditor has misunderstood the evidentiary review in this case, and that there has been no computational error in the assessment of the evidence."*

81. In OIOS' view, the Secretariat has misunderstood the audit recommendation. OIOS did not question the classification of evidence by the Panel or that there was a calculation error. Instead, OIOS has requested the *"complete details (along with working papers) of the sample check conducted by the consultants on the basis of which the Damage Assessment Report is classified as primary evidence of loss or damage and the Quantity of evidence has been classified as complete."* Therefore, the Secretariat has not explained why details of the sample check, asserted to have been conducted by the consultant, cannot be provided.

Recommendation 11

The Secretariat should provide OIOS with the complete details along with the relevant working papers of the sample check conducted by the consultants on the basis of which the Damage Assessment Report is classified as primary evidence of loss or damage and the quantity of evidence has been classified as complete regarding Claim No. 5000192 (AF02/27/3/011).

Real property losses

82. Since all repairs and replacements of damaged buildings were undertaken subsequent to July 1991 the claimant should have submitted copies of the original contracts, invoices, and payments made to the contractors, etc. However, these were not attached to the claim documents submitted. It appears that the consultant obtained and reviewed some of these documents (refer Appendix 2 to the consultant's final report). OIOS requested the Secretariat in audit observation recommendation no. AF2002/27/3/127 to provide the documents referred to in Appendix 2 of the consultant's final report. These documents (Appendix 2 -Reference 5000 – 5031) have not been provided. Instead the Secretariat provided a different document (the Brown & Root proposal), referred to in another OIOS recommendation (no. AF2002/27/3/130).

Overlapping claim for repair of aircraft shelters

83. The Claimant stated that the cost to repair the destroyed aircraft shelters was not included in the December 1991 Master Plan cost estimate. Accordingly, it claimed KD23.33 million (\$77.56 million) for this loss based on the proposal prepared by Brown & Root and another contractor.

84. We observed that the December 1991 Master Plan Cost estimate included \$66.98 million for the repair and construction of new aircraft shelters. Furthermore, \$22.38 million was provided in the estimate for replacing aircraft hangars. The total amount in the estimate for this purpose was \$89.37 million (\$66.98 million+ \$22.38 million). Since the claims in the Brown & Root proposal and the Master Plan cost estimates refer to the similar aircraft shelters these may be overlapping claims unless there is evidence to the contrary.

85. UNCC noted that: *"The secretariat therefore considers that the auditor's concern that there may be an overlap between the aircraft hangars included within Estimate and the "Hardened Aircraft Shelters" included in the Brown and Root estimate is unfounded."*

86. We note the following deficiencies in the Secretariat response:

- Although the Secretariat provided the Brown & Root proposal, it did not include the cost proposal and as a result we were unable to confirm the costs proposed by Brown & Root.

- The Secretariat's assertion that the \$66.98 million was not included in the claim was a presumption and not a fact. No specific evidence has been provided that the cost stipulated in the Master Plan cost estimate was excluded and the reasons therefore. There were also other discrepancies as to the cost for helicopter Hangar nos. 12.1 - 12.3 which have been estimated twice - the cost was included both for the U.S. contractor (70 per cent Facility) and for the MoD local contractors (30 per cent Facility list). Additionally, the claimant claimed \$100.9 million for damage assessment, restoration design, construction management, and construction of air bases.

87. As a consequence, the claimant has been overcompensated by approximately \$64 million (UNCC adjusted the claim of \$77.56 million by 17.5 per cent; although they should not have awarded any compensation). These problems have arisen because the consultant and the Secretariat processed the claim on the basis of estimates instead of original invoices/payments. As the repairs and replacements took place after the Iraqi invasion, the claimant should have submitted original invoices or payments details in support of this claim. However, no such documents are available. The consultant and the Secretariat should have requested the original invoices/payment details. In the absence of these original documents the classification of evidence should have been adjusted appropriately. However, we note that the consultant has classified the evidence as shown in Figure 11:

Figure 11: Classification of Evidence by Consultant

Evidence Factor	Result	Reason	Paragraph reference
Period of occurrence	Post emergency	Visit undertaken September 2000	5.7
Type of evidence	Primary	Independent visit	5.7
Quantity of evidence	Partial & supported	Not all property seen. Some structures demolished and site cleared prior to inspection	5.7
Quality of evidence	Good	Good evidence provided	5.7
Factor	17.5%		

88 The type of evidence has been classified as "primary" on the basis that the consultant made an "independent visit". The basic evidence required was the original invoices/payment details for repair and replacement and not for an "independent visit" ten years later. Since the repair and replacement took place after the invasion, the claimant should have provided copies of the invoices/payments for the latter. However, there was no explanation of why the original invoices were not submitted. In the absence of such original invoices the evidence factor should have been appropriately adjusted. OIOS believes that failure to do so resulted in overcompensation to the claimant.

Recommendations 12 and 13

Regarding claim no. 5000192, the UNCC Secretariat should make adjustments in compensation awarded for real property losses due to:

- (i) The failure of the claimant to submit original invoices/payment details by amending the ESM factor for inadequate evidence (AF02/27/3/012); and
- (ii) The duplicate claims compensated for aircraft shelters (AF02/27/3/013).

Hawk air defense system: Inadequate evidence for reimbursement of claim

89 The claimant asserts that components of the Hawk Air Defence System were not returned by Iraq and claimed \$450million for this loss. The only evidence provided by the Claimant was an "internal pre-invasion Ministry of Defence document listing the amounts spent on the I-11 Hawk system." The document is a schedule of purchases from 1976 to 1988. Even though the total amount of purchases exceeded \$367 million, details of the items or services procured were not available. Considering the amount involved, the Claimant should have provided details of items or services procured or the Secretariat should have requested these details in order to process the claim.

90. OIOS observed that the procurement referred to repeated purchases of a few items. The Claimant spent more than \$220 million on "Hawk Omnibus" and \$87 million as "Hawk Support" during the period. However, details of what was actually procured with these amounts were not available. The Secretariat appears to have considered that all procurement (excluding \$11.6 million for spares, repair & rebuild, which had been adjusted, was for component parts and hence compensable. However, this sophisticated electronic equipment requires substantial support for operations, logistical support and maintenance. It is possible that this huge expenditure on the Hawk system may have been incurred for both hardware items as well as logistical and technical support services.

91. OIOS observed that "Raytheon", the manufacturer of the Hawk system, provides products and services in the areas of commercial and defence electronics. The services provided include scientific, technical and professional services, repair and supply depot operations; engineering, logistics and personnel support; range support; etc. The Raytheon website shows that one of the Integrated Logistics Support services provided by the company was "Hawk support".

92. Thus the available evidence suggests that the \$87 million for "Hawk support" was spent on Integrated Logistics Support services, which was a service and not procurement of parts, or equipment that forms part of the system. As this cost was incurred for technical or logistic support services, etc., and the services were availed, the claim is not compensable.

No evidence of amount paid

93. According to the evidence submitted (Exhibit 16) \$4.79 million was outstanding and not paid by the claimant to the vendor. Since there was no evidence that this amount was subsequently paid, the amount should be reimbursed by UNCC only if the claimant can provide evidence that the amount was actually paid to the vendor.

94. The Secretariat noted that: *"Accordingly, the secretariat concludes that there is no evidence to suggest that the amount of compensation recommended included any element of costs that would not have been sustained in replacement of the destroyed system, and so that no alteration to that amount should be made."*

95. The Secretariat's response is not tenable for the following reasons:

- The Secretariat advised that the claimant *"confirmed that it could not confirm the detail contained in Exhibit 16 was complete"*. Considering the claim amount exceeded \$300 million, and given the absence of any evidence, the consultant (or the Secretariat) should have requested additional evidence and written clarification from the claimant as in other claims. However, neither written evidence nor clarification was obtained, and the claim was processed based on the asserted discussions with the claimant during the consultant's visit.
- The Secretariat asserted that Kuwait purchased the system for \$4.7million in 1974 and that the \$78.8 million incurred in August 1977 included costs for part of the original system, a major initial upgrade to the system and other related costs. Normally, significant sums are incurred either for the original purchase or for upgrading but not for both. It is unusual that the \$78.8 million incurred in August 1977 included costs for both the original system and the upgrade. It is also unusual that before the original system was procured and installed the claimant proceeded with an up-grade. Further, the nomenclature of the costs-- "Hawk Support" implies that this cost related to support, maintenance or provision of essential services and not to original procurement. Further, as pointed out above (paragraph 90) the original manufacturer of Hawk provides Integrated Logistics Support services, which include "Hawk Support". Therefore all available evidence leads to the conclusion that the claimant incurred the costs for logistic support services and not for procurement or up-grading the equipment.
- The Secretariat also explained that the "Hawk Omnibus" costs of \$220million related to major modifications and upgrades of the system. These modifications and up-grades are normally made after a period of time following original procurement. However, the Secretariat's assertion implies that the Hawk system was significantly upgraded annually from 1981 to 1984 as shown in the Fig.12 below:

Fig. 12 Statement showing claim for Hawk Support and Hawk Omnibus

Case no.	Description	Date Signed	Amount Paid
KU-B-UAH	HAWK SUPPORT	09-08-1977	\$78,777,283
KU-B-UGA	Hawk omnibus	14-12-1981	69,485,343
KU-B-UFG	Hawk omnibus	27-3-1982	92,873,760
KU-B-UGW	Hawk omnibus	10-10-1984	57,878,922
KU-B-KRB	HAWK SUPPORT	05-08-1985	3,000,000
KU-B-KRC	HAWK SUPPORT	23-12-1986	1,369,543
KU-B-KRE	HAWK SPT (FMSO II)	02-09-1987	2,987,625
KU-B-KRF	HAWK SUPPORT	29-11-1988	1,000,000

- Although the Secretariat asserts that the costs incurred for "Hawk Support" and "Hawk Omnibus" were for modification and upgrades, it has not considered that these costs could include logistic and support services. Typically, in such contracts, services like technical training, testing and maintenance are included.
- The Secretariat stated that adjustments were made for compensation of support costs that were recurring in nature (paragraph 134). However, OIOS noted from the consultant's final report that adjustments were made for spares and repairs & rebuild only (latest adjustment made related to 1983). Hence, the claimant made no adjustments for recurring maintenance, training and logistic support costs incurred from 1977 to 1990. Considering the sophisticated nature of the equipment and the repeated upgrades, the support costs would have been substantial. However, no adjustments have been made for savings of maintenance and support costs.
- The claimant supported its claim of \$450million with a two page document listing the purported purchases and payments. However, this document, which was maintained by an external case manager, and not by the claimant, did not provide independent evidence of what items or services were procured, the original purchases made, the terms and conditions of purchase, etc. The Secretariat now asserts that this deficiency was discussed with the claimant, and based on the claimant's explanation, UNCC processed the claim for compensation. Considering the amount involved was \$450 million, the Secretariat should have obtained a written explanation to ensure transparency in processing the claims. The Secretariat has not explained why it did not require this written clarification.

96. The Secretariat did not respond to OIOS' query as to whether the outstanding amount of \$4.79 million was paid by the claimant to the vendor. In light of the above there is inadequate evidence for the compensation of \$214.9 million (refer to paragraph 89 and 92).

Recommendations 14 - 15

OIOS reiterates its recommendation regarding claim no. 5000192 calling for the UNCC Secretariat to recover the following amounts paid in compensation:

(i) \$307 million claimed for Hawk Omnibus and Hawk Support costs as the claimant did not submit details of purchases made and there was no evidence that it purchased equipment with this amount (AF02/27/3/014); and

(ii) \$4.79 million claimed for the Hawk Air Defence System as there was no evidence that the claimant paid this amount to the vendor (AF02/27/3/015).

Inadequate evidence for compensation of the missile re-loader system

97. Our review of the \$39.4 million claim for a missile re-loader system showed that the claimant had not provided evidence showing: (i) it owned the system; (ii) the basis for assessing the damages to the system at \$39.4 million; and (iii) it was procured in 1987. There was also no reference in the consultants' final report indicating whether they had reviewed evidence concerning the existence of the system and the damage done to it. OIOS therefore requested the Secretariat to provide documents and other evidence considered in compensating the claim for the system.

98. *The Secretariat responded: "The auditor appears to have overlooked the discussion of the witness statement of Lieutenant Colonel Hazza Al-Hazza of the Kuwait Air Force (Exhibit 3 to the claim), which addresses both the existence and loss of the entire element at issue (an amount of \$1,626,709,000 for "Military assets", of which the system at issue comprises \$39.4 million). The adjustment was made using the ESM as described in paragraphs and amounts to 10 times the asserted value of loss to the missile re-loader system itself."*

99. The Secretariat's response is not tenable because:

- i. The claimant's assertion is not independent evidence of the system's existence. The claims made by the claimant have to be verified independently, which is the basic purpose for retaining the consultant.
- ii. *The Secretariat claimed that "further enquiries to support the evidence in that report were not undertaken for this system, as it is less than 2.5 per cent of the total value of the loss element". OIOS does not agree with this reply because the \$39.4 million*

involved substantially exceeds the materiality amount of \$500,000 proposed by the consultants²⁰ and approved by the Panel. In this regard, the consultant verified the loss in the claim for books and libraries in the amount of \$5.5million in the same claim (no. 5000192). Therefore, in OIOS' view, the consultant and the Secretariat should have verified evidence for the existence of the missile re-loader system, as there is no evidence or justification for awarding compensation of \$27.3 million²¹.

Recommendations 16

OIOS reiterates its recommendation that the UNCC Secretariat adjust the compensation awarded under claim no. 5000192 for the missile reloader system since there is no independent evidence substantiating the existence and loss of this system (AF02/27/3/016).

Overcompensation due to the failure to convert Kuwaiti Dinars into US dollars

100. The claim for the missile re-loader system was in Kuwaiti Dinars and not converted into US dollars. Therefore, the depreciation was short by approximately \$3 million. OIOS therefore recommended that compensation be adjusted to address this error.

101. The Secretariat agreed with OIOS that there was a calculation error and that depreciation was short by \$3 million. They clarified that: *The depreciation has been re-calculated on this basis, giving an adjustment of \$3,943,000, as compared with that previously recommended of \$1,779,000. The overstatement in the amount recommended is \$2,164,000, which after application of the ESM is reduced to \$1,515,000*²².

Maintenance expenses saved but no adjustment made

102. The claim had not been adjusted to reflect savings in maintenance expenses for the missile re-loader system had not been adjusted. OIOS therefore recommended that these savings be considered in the claim amount.

103. The Secretariat responded: *"The consultants advise that savings in maintenance expenditures were accounted for in combination with the LASS system. The consultants applied a standard maintenance cost saving per annum on each of the individual air defence systems (including the missile re-loaders) that formed part of this loss element*²³*. The amount of that adjustment does not change even if the missile re-loaders are considered as part of the Amount and not the LASS system."*

²⁰ Guidelines for the Application of Evidentiary Standards Preliminary Report to the F3 Panel & Secretariat (paragraph 1.29)

²¹ Net compensation awarded by UNCC for the missile re-loader system

²² Calculated as overstatement (correct depreciation \$3,943k less depreciation calculated in the Final Report \$1,779k = \$2,164k less ESM factor 30 per cent) = \$1,515k.

²³ It should be noted that the loss element included a less sophisticated system, the Strela system, which had a lower annual maintenance cost and, accordingly, saved expenses were not adjusted at the standard rate for the Strela system.

104. The Secretariat asserted that the savings were accounted for with the LASS²⁴. However, OIOS' review revealed that the consultant's calculations for savings in maintenance relate to the LASS only and does not include the savings for missile reloader system. The Secretariat also informed OIOS that the consultant accepted that they had incorrectly linked the missile reloaders to the LASS. Instead the missiles were purchased to improve the efficiency of the Amoun system. However OIOS noted that no evidence has been made available to confirm that the missiles were purchased to improve the efficiency of the Amoun system. Thus failure to provide savings has resulted in overcompensation of approximately \$2 million.

Recommendations 17

OIOS reiterates its recommendation that the UNCC Secretariat adjust the compensation awarded under claim no. 5000192 to reflect the savings in maintenance expenses for the missile reloader system (AF02/27/3/017).

Payment of relief to others: back salaries of military personnel, contractors and technicians

105. The claimant sought compensation in the amount of \$407.5 million for relief paid to MOD employees (including military personnel). The UNCC awarded \$41.1 million after making adjustments. OIOS' review of this claim revealed that the Panel of Commissioners at its 6-7 June 2001 meeting decided that:

- a) Back salary payments to MoD employees and National Guard (NG) members who were outside Kuwait (in Saudi Arabia for example) on active duty, including duty as part of the allied coalition forces, are not compensable.
- b) Back salary payments for the occupation period to MoD employees or NG members, who were in Kuwait during the occupation and engaged in resistance activities, are compensable.
- c) Back salary payments to MoD employees or NG members, who were neither on active duty outside of Kuwait, nor engaged in resistance activities in Kuwait during the occupation, are compensable.
- d) For the emergency period, back salary payments to NG employees in Kuwait are not compensable to the extent that they were paid to individuals who performed the tasks for which they were employed.

106. The above decisions were based on the reasoning stated in the 34th Briefing Note submitted by the Secretariat to the Panel. However, the specific reasons for the decisions in items (b) and (c) were not apparent from the Briefing Note. Furthermore, although the MoD claim was for "Occupation period salaries" the Secretariat considered this claim as "Ministry of Defense seeks compensation for the relief paid to its employees for the seven month occupation period....". According to the Secretariat if these payments were classified as "salaries" then there is no basis

²⁴ Low Altitude Surveillance System

upon which the compensation could be awarded. The claim could only be considered if the payments made by Kuwait were classified as "relief".

107. The Governing Council decided that "...the costs of the Allied Coalition Forces, including those of the military operations against Iraq, are not eligible for compensation" (Decision 19). As the military personnel who were in Kuwait during the occupation, and involved in resistance against Iraq (referred to in paragraph 99) were trained professional soldiers, the resistance provided by them amounts to a military operation against Iraq. The back salary (or the relief) paid to these employees is a cost to Kuwait and appears to be covered by the GC decision 19. Hence, in OIOS' view, the back salaries/relief paid to these military personnel is not eligible for compensation.

108. War is the business of military personnel, and their activities do not come to a standstill during war time, unlike other civil employees who may be unable to perform their normal tasks. It is also likely that in war time conditions, soldiers are cut off from the main chain of command, and are behind enemy lines and still resist the enemy. Thus, the military personnel in Kuwait involved in resistance activities were, in our view, performing their duties. Furthermore, since these were professionally trained soldiers, the resistance they provided would be more effective than the resistance provided by the ordinary citizens acting on their own. Thus, it appears that Kuwait has received the benefit of the services of military personnel who were involved in resistance and thus has an obligation to pay for their services. In OIOS' view, the relief paid by Kuwait to these "employees", does not appear to be compensable.

109. The Secretariat responded: *"The secretariat is of the view that the recommendations extend into an area that is, according to the OLA opinion, beyond the proper scope of an audit query. Interpretation and application of Governing Council decisions, assessment of evidence and findings of facts are all matters within the exclusive jurisdiction of the Panels of Commissioners and are not amenable to audit.* However, as discussed in paragraph 5 of this report, OIOS does not agree that its recommendation extends into an area beyond the scope of OIOS' audit authority

Tangible property - spare parts

110. The total claim for the spare parts was \$46.15 million, and the amount recommended was \$38.07 million. The consultants utilized the evidence in their working paper # 6547 for applying the ESM. OIOS observed that there was a discrepancy in the classification of the ESM factor derived from their working paper. The Secretariat responded that the *discrepancy was a clerical error and that there was no financial impact.* While OIOS agrees that there was no financial impact, the records should be revised to reflect the correct classification.

F. Other matters and conclusions

Attachment of confidential material to the memorandum

111. During the review of claim no. 5000192, the OIOS auditor issued audit notes to the UNCC Secretariat seeking clarifications on the work performed by the consultant. As OIOS observed a

calculation error in the consultant's working paper – OIOS attached the consultant's working paper to one such note for ease of reference.

112. In this regard, the Secretariat stated that "*(it) notes with concern that confidential documents from the claim files/consultants' working papers have been attached to the memorandum. Article 30(1) the UNCC's Provisional Rules for Claims Procedure (the "Rules")²⁵, provides that all records received or developed by the Commission will be confidential. The secretariat requests that the final audit observations be issued without such attachments and that OIOS certify that no copies of the draft observations have been disseminated beyond the UNCC, nor have been handled otherwise than in accordance with article 30(1) of the Rules.*"

113. In OIOS' view, the Secretariat's concerns are unwarranted. In a subsequent meeting, the OIOS auditor reassured the Secretariat and senior management that draft observations had not been disseminated outside of the Secretariat.

Conclusions

114. As discussed above, OIOS audit of selected F-3 claims raised a series of questions concerning the awards made by the Secretariat, which in OIOS' view resulted in substantial overcompensation of the claimants. As the Secretariat's responses have not fully addressed these concerns, OIOS believes that it is imperative for the UNCC to re-examine the issues discussed in this report, and adjust the amounts of compensation awarded in these claims.

Recommendation 18

OIOS recommends that the UNCC Secretariat apprise the Governing Council of the above OIOS recommendations for their consideration and appropriate action (AF02/27/3/18).

VI. ACKNOWLEDGEMENT

115. We wish to express our appreciation for the assistance and cooperation extended to the auditor by the Secretariat.

Patricia Azarias, Director
Internal Audit Division I, OIOS

²⁵ Document S.AC.26/1992/10.